

**REPORT OF THE AUDITOR-GENERAL TO THE MUNICIPAL COUNCIL AND KWAZULU-NATAL PROVINCIAL LEGISLATURE ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF HIBISCUS COAST MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2007**

**REPORT ON THE FINANCIAL STATEMENTS**

**Introduction**

1. I have audited the accompanying financial statements of the Hibiscus Coast Municipality which comprise the statement of financial position as at 30 June 2007, statement of financial performance, statement of changes in net assets, and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages 3 to 36.

**Responsibility of the accounting officer for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the basis of accounting determined by the National Treasury, as set out in accounting policy note 1 and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA). This responsibility includes:
  - designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
  - selecting and applying appropriate accounting policies
  - making accounting estimates that are reasonable in the circumstances.

**Responsibility of the Auditor-General**

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004)(PAA) read with section 126(3) of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

### **Responsibility of the Auditor-General (continued)**

6. An audit also includes evaluating the:
  - appropriateness of accounting policies used
  - reasonableness of accounting estimates made by management
  - overall presentation of the financial statements.
7. Paragraph 11 et seq. of the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of Financial Statements* requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is still in the process of being developed, I have determined that my audit of any disclosures made by Hibiscus Coast Municipality in this respect will be limited to reporting on non-compliance with this disclosure requirement.
8. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

### **Basis of accounting**

9. The municipality's policy is to prepare financial statements on the basis of accounting determined by the National Treasury as set out in accounting policy note 1 to the financial statements.

### **Basis for qualified opinion**

#### **Accounts Payable**

10. The municipality could not provide evidence to support accounts payable balances amounting to R7,6 million.

Consequently, we could not verify the accuracy and completeness of accounts payable.

### **Qualified opinion**

11. In my opinion, except for the effects of the matters described in the Basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of Hibiscus Coast Municipality as at 30 June 2007 and its financial performance and cash flows for the year then ended, in accordance with basis of accounting and in the manner required by the MFMA.

### **Emphasis of matter**

I draw attention to the following matters

### **Basis of accounting (departures and deviations)**

12. The National Treasury approved a deviation from the basis of accounting applicable to municipalities on 31 July 2007, which granted the municipality exemption relating to Employee benefits – IAS 19 (AC 116). The exemption related to the defined benefit accounting as far as it relates to defined benefit plans accounted for as defined contribution plans and the defined benefit obligation disclosed by narrative information. [paragraphs 29, 48 – 119, 120A(c) -(q)].

Therefore, the municipality has adopted and applied IAS19 (AC 116).

## **OTHER MATTERS**

I draw attention to the following matters that are ancillary to my responsibilities in the audit of the financial statements:

### **Non-compliance with applicable legislation**

#### **Municipal Finance Management Act (MFMA)**

13. The municipality has not developed and implemented a fraud prevention plan and risk management policy. The municipality has therefore not effectively managed its risk in accordance with section 62 (1) (c) (i) of the MFMA.

#### **Municipal Systems Act (MSA)**

14. Certain councillors did not declare all their business interests as required by section 5 of schedule 1 (code of conduct for councillors) of the MSA, Act No 32 of 2000.

#### **Division of Revenue Act**

15. The municipality does not maintain separate bank accounts for capital replacement reserve in compliance with accounting policy note 5.

### **Material corrections made to the financial statements submitted for audit**

16. The financial statements, approved by the accounting officer and submitted for audit on 31 August 2007, have been revised in respect of the following misstatements identified during the audit:
  - 16.1. Accounts payable was overstated and investments understated by R9,8 million due to the interest on investments been incorrectly processed against creditors. The financial statements were adjusted to reflect the correct allocation.
  - 16.2. Long term liabilities were overstated and creditors understated by R4,4 million as loan repayments were incorrectly processed against creditors. The financial statements were adjusted to reflect the correct allocation.
  - 16.3. IAS 39 (AC 133) Financial Instruments: Recognition and Measurement was not applied to the outstanding cheques at year end resulting in the understatement of cash and bank as well as creditors by R19,1 million.

- 16.4. The Provision for Landfill site rehabilitation has not been raised in terms of IAS 19. This resulted in an understatement of the provision and expenditure accounts of R11,6 million. These amounts were adjusted accordingly.
- 16.5. Loan repayments have been incorrectly processed against creditors. As a result the long term liabilities were understated by R16,2 million and creditors, interest on loans and accumulated surplus overstated by R4,4 million, R184 000 and R7,2 million, respectively. These amounts were adjusted accordingly.
- 16.6. Resulting from misallocations of certain expenses it was found that general expenses have been overstated by R2,5 million and salaries, other income and accumulated surplus understated by R1 million, R600 000 and R905 000, respectively. These amounts were adjusted accordingly.
- 16.7. Remuneration of councillors and general expenses were overstated by R1,5 million and R 905 000 respectively resulting in accumulated surplus been understated by R2,4, million due to prior year expenditure expensed in the current financial year. The financial statements were adjusted to reflect the correct allocation.
- 16.8. Accumulated surplus was overstated by R2,8 million and the inter-municipal account balances for Ugu–District municipality (reflected as a credit balance) and the long term debtors understated by R1,9 million and R987 000, respectively. The financial statements were adjusted to reflect the correct allocation.

### Internal control

17. Section 62(1) (c) (i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes of the matters indicated, as they relate to the five components of internal control.

Reporting item	Control environment	Assessment of risks	Control activities	Information and communication	Monitoring
<b>Basis for Qualification of opinion</b>					
Accounts Payable			✓		
Non-compliance with MFMA	✓				
Non-compliance with MSA			✓		

Reporting item	Control environment	Assessment of risks	Control activities	Information and communication	Monitoring
Non-compliance with DORA			✓		

### Unaudited supplementary schedules

18. The supplementary information set out on pages 37 to 41 does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly I do not express an opinion on them.

### OTHER REPORTING RESPONSIBILITIES

#### Reporting on performance information

19. I have audited the performance information as set out on pages xx to xx.

#### Responsibility of the accounting officer for the performance information

20. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

#### Responsibility of the Auditor-General

21. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 646 of 2007*, issued in *Government Gazette No. 29919 of 25 May 2007* and section 45 of the MSA.
22. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
23. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

#### Audit findings (performance information)

#### Functioning of a performance audit committee

24. The audit committee functioning as a performance audit committee did not meet at least twice during the financial year to review the quarterly performance reports submitted by the internal auditors and did not review the municipality's performance management system to make recommendations in this regard to the council of Hibiscus Coast municipality.

### **Late finalisation of the audit report**

25. In terms of section 126 (3) (b) of the MFMA the Auditor-General is required to submit the audit report to the accounting officer within three months of the receipt of the financial statements. In the interest of improving accountability and due to the process implemented to ensure consistency in the manner in which material audit findings are reported, I have delayed the finalisation of the audit report to the date reflected on the audit report.

### **APPRECIATION**

26. The assistance rendered by the staff of the Hibiscus Coast Municipality during the audit is sincerely appreciated.

*Auditor-General*

Pietermaritzburg

10 March 2008



A U D I T O R - G E N E R A L